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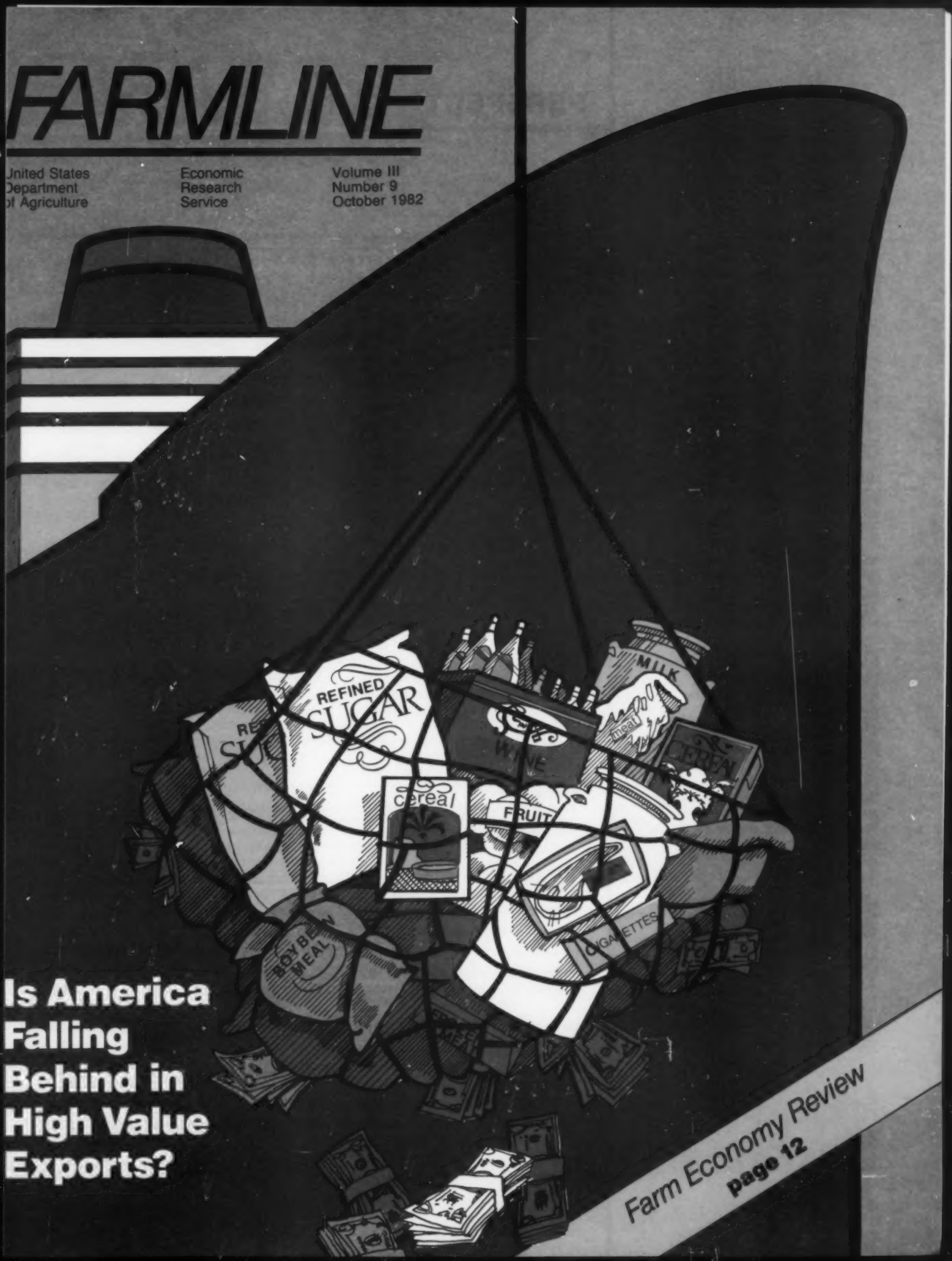

Is America Falling Behind in High Value Exports?

Farm Economy Review
page 12

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PERSPECTIVES

USDA's 1982 farm income forecasts are in. They point to a drop in overall cash receipts from 1981 (as lower crop receipts offset record livestock receipts), a sharp rise in government payments, but higher production expenses, too. Bottom line: Net farm income about $19 billion, the lowest since 1977. See page 14 for more on farm income.

	1979	1980	1981	1982*
	billion dollars			
Cash receipts:				
Crops	63.1	71.7	75.0	70–74
Livestock	68.6	67.8	68.5	68–72
Total	131.7	139.5	143.5	140–144
Direct government payments	1.4	1.3	1.9	4.0–4.5
Other farm income[1]	12.6	14.1	15.8	16–18
Total gross income	145.7	154.9	161.2	161–165
Total production expenses	119.0	130.5	141.6	142–146
Net farm income before inventory adjustment	26.7	24.4	19.6	17–21
Value of inventory change	+5.6	−4.3	+5.5	−1–+1
Net farm income after inventory adjustment:				
Current dollars	32.3	20.1	25.1	17–21
Deflated (1972) dollars[2]	19.9	11.4	13.0	8–10

*1982 forecast
[1] Income from recreation, machine hire and custom work, imputed rental value of operator dwellings, and value of farm products consumed on the farm. [2] Deflated by the GNP implicit price deflator.

Storage pressures mount as harvests shift into high gear. A special analysis of 16 major storage states indicates that on-farm storage will be very tight during harvests, except in Oklahoma, North Dakota, and Nebraska. But only Indiana and Ohio are expected to face severe storage problems. As usual, overall numbers show excess U.S. capacity, but the bins aren't always where the crops are.

Sales of production inputs continue to lag as farmers trim costs wherever they can. Pesticide sales slipped about 4% this year, the first decline in 20 years. Farm use of fertilizers will drop more sharply--perhaps about 8% for nitrogen, 12% for potash, and as much as 25% for phosphate fertilizers. Machinery sales remain very weak and may be off 25% or more for the year. Sales dropped 13% last year and 20% in 1980.

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Is America Falling Behind in High Value Exports? *by Patricia F. Singer* 4

We export more farm products than ever, but our share of the world trade dollar has lagged. Why? Most U.S. agricultural exports are raw, bulk commodities such as grains, while many exporting nations now specialize in processed and other high value products which bring much greater returns per ton. According to economist Pat O'Brien, we'll have to become more aggressive marketers if we want a bigger share of this blue chip trade.

U.S. Beef: Pricing Itself Out of Mideast Markets *by Daniel R. Williamson* 8

While the growing global appetite for beef is creating thriving import markets, American producers are missing the boat because their top-grade, feedlot-finished meat is too expensive. In the Mideast, a prime example of an area where meat demand has surged, high-priced U.S. beef is a specialty product sold mostly to foreigners, says economist John Parker.

Up and Down Business Cycles Now Rock Rural Economy *by Lloyd D. Bender* 9

The "sleepy village" image of rural towns may mask an economic revolution that is binding the prosperity of rural America ever more closely to swings in the overall U.S. economy. Economic diversification, growing dependence on nonfarm jobs, and closer links with national money markets are some of the factors that are quickly eroding the historic economic isolation of rural counties.

A Vintage Time for American Wine? *by Sherrie Meyer* 10

Americans are raising their wine glasses more often, and the U.S. wine industry has expanded to meet the growing demand. Although foreign competition remains a big concern as imports capture a larger share of the U.S. market, Americans still prefer the home-grown product by far. One unanswered question is how well U.S. wines can compete abroad. Our exports are small, but they're growing fast.

Lean Years for U.S. Farmers *by Leland Scott* 12

How serious are economic conditions in the farm sector, and how did they get that way? Some recent statistics and a review of the last few years provide some answers. In simple terms, the erosion of farmers' financial well-being since 1979 reflects the failure of farm prices to keep pace with rising costs. But large supplies, weak demand, high interest rates, the jump in oil prices, and even a drought and a grain embargo are all part of the picture.

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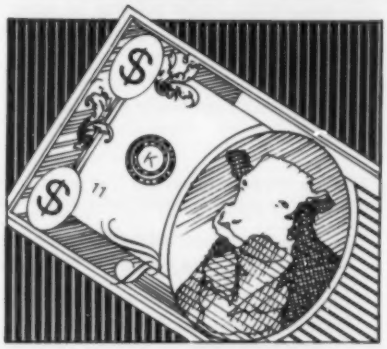


Is America Falling Behind in High Value Exports?

The United States is exporting more agricultural products than ever, but America's share of the world agricultural trade dollar has shown relatively little growth over the last decade.*

Why? Most U.S. agricultural exports are unprocessed products sold in bulk, such as grains, while many other exporters are specializing in higher value products, processed and unprocessed. Since 1970, these high value products (HVP's) have accounted for more than half the growth in the value of world agricultural trade, according to economist Pat O'Brien of USDA's Economic Research Service.

A major reason is the rapid increase in HVP prices. In the last decade, export prices for HVP's rose an average of 10-14 percent a year, more than enough to make up for moderate volume gains that didn't always keep pace with expanding trade volume in other farm products. As a result, HVP exporters were able to capture a larger share of the world trade dollar, even while supplying a smaller share of total trade volume.

In contrast, exporters of low value, bulk products (LVP's) watched their share of world trade earnings decline, despite a larger share of volume. While the U.S. sharply expanded its percentage of the LVP market at the expense of rival exporters, much of the growth in the more profitable HVP market went to other suppliers.

From 1970 to 1980, the U.S. share of total world farm trade volume rose from about 25 percent to 40 percent. However, our share of trade value reached only 18 percent.

"The unprecedented gains the United States enjoyed in the world LVP market over the 1970's tended to distract attention from equally impressive growth in HVP trade," O'Brien says.

HVP exports accounted for slightly more than half the total value of world agricultural trade by 1980, up from 44 percent in 1970.

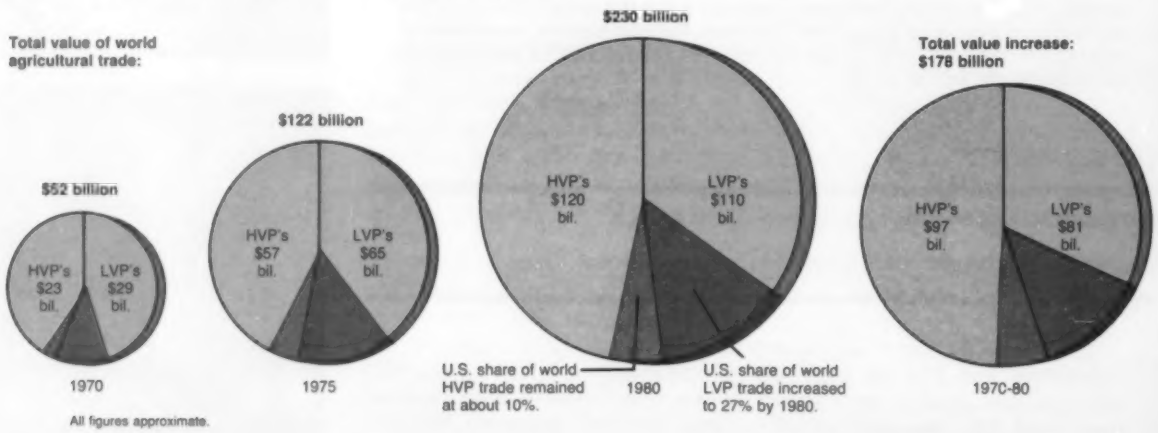
All About HVP's

HVP's can be divided into three groups:

- Semiprocessed products, such as fresh and frozen meats, flour, vegetable

*The U.S. share actually shrunk if all products processed from farm commodities are counted in trade value totals.

High Value Products Accounted for More Than Half of the Growth in Value of World Agricultural Trade from 1970-80 . . . But the U.S. Share of HVP Trade Remained Relatively Small



All figures approximate.

meals and oils, roasted coffee, refined sugar, and cocoa products. By the late 1970's, about half of the world's $120 billion worth of HVP trade was in semi-processed products.

• Highly processed products that are ready for the consumer, such as milk, cheese, breakfast cereals, wine, and cigarettes. About one-third of world HVP trade was in this type of product by 1980.

• High-value unprocessed products that are also often consumer-ready, such as fresh and dried fruits and vegetables, eggs, and nuts. One-sixth of world HVP trade at the end of the 1970's was in these items.

When HVP's are exported, they bring in much greater returns than comparable amounts of raw, bulk commodities. O'Brien says that the export value of HVP's may average $1,000 to $1,500 a ton, whereas LVP's may be worth only $200 to $300 per ton, or less. The export value of corn, for example, is currently $110-$120 a ton.

The value that's added in processing most HVP's spells increased employment and income for the exporting country. For this reason, many U.S. trade associations, labor groups, and government trade specialists have been stressing that lucrative HVP exports have great potential for creating jobs and bettering our balance of trade.

Those who advocate a push to expand HVP exports also emphasize, however, that they don't want to see HVP exports grow at the expense of America's LVP trade. Instead, they want to see that processed exports complement the nation's massive trade in raw commodities.

Indeed, after the European Community (EC), the United States is already the leading HVP exporter in the world, with a 10-percent share of global trade. Although the EC has the lion's share—45 percent—almost two-thirds of its sales are made within the Community.

U.S. exports of HVP's in calendar 1981 were worth about $12 billion. Our LVP exports last year totaled $30 billion. Thus, of our total agricultural exports in 1981, HVP's represented about 30 percent and LVP's about 70 percent.

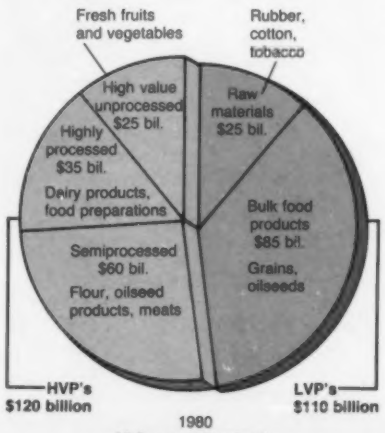
Growth in U.S. Exports of HVP's

The preponderance of our LVP exports perhaps obscured the expansion in our HVP exports—about 17 percent a year between 1970 and 1980, according to O'Brien.

Much of the growth was due to increased buying by oil-rich OPEC nations. In 1970, OPEC countries were taking about 4 percent of our HVP exports. By 1980, they were buying 9 percent. U.S. poultry and cigarettes, especially, grew in popularity among OPEC consumers.

Other large U.S. customers include Japan, Canada, and the EC. Together, the three account for more than half of our HVP export sales. Major U.S. products that the three import are oilseed meals (EC), meat (EC and Canada), and fresh fruit (Japan, EC, and Canada).

Major HVP and LVP Components of World Agricultural Trade



All figures approximate.

It may seem odd that the European Community is both our leading competitor and our leading customer for HVP's. But that, says O'Brien, points up one of the chief characteristics of the world market. The biggest HVP exporters—the United States, the EC, and Brazil—are also major HVP consumers. They produce many diverse HVP items for their own large domestic markets, as well as for export.

Most other nations that export significant amounts of HVP's specialize in fewer products. The products tend to be items in which the countries have a natural advantage or a processing cost advantage, or—in a limited number of cases—items that have received special government encouragement, such as export subsidies. Countries in this second category include Australia and New Zealand, which specialize in livestock products; Spain, in citrus fruits; Mexico, in fresh vegetables; and Canada, in meats.

The world market for HVP's differs from the LVP market in numerous ways, according to O'Brien. Among the differences:

• There are 300 to 400 HVP's traded on the world market, in contrast to 20 to 30 LVP commodities.

• More countries export HVP's than export LVP's. And, O'Brien notes that "every country in the world imports some HVP's."

• A greater portion of the return on an HVP export usually goes to the processor, for value added, than to the farmer, who may get only 10 to 15 percent. A ton of cheese, for instance, may bring an export return of $2,900 a ton, with roughly $2,300 (or 80 percent) going to processors and $600 (20 percent) going to farmers. With LVP's, the farm sector usually gets 60 percent or more of the return, and the processors and marketers as little as 20 or 30 percent.

• Because HVP's are more expensive to transport than LVP's (HVP's often require special handling or refrigeration),

geography plays a greater role in giving an exporting country a trade advantage. For example, Brazilian poultry producers have a geographical edge in selling to markets in Chile, Central America, and the Caribbean.

• The HVP market has grown more steadily than the mercurial LVP market.

• Vertically integrated, multinational corporations are more likely to be involved in HVP trade, because they can easily shepherd an item from its production and processing in one country to its final marketing in another. LVP trade tends to be dominated by a few companies that handle only international marketing.

For the Future

What's the future of HVP trade, especially the U.S. slice of it?

O'Brien says that the U.S share of the world market could be expanded from 10 to possibly 15 percent by 1990. Even if the U.S. share held constant, we would reap larger HVP earnings because worldwide trade in HVP's is also expected to grow—though the growth rate may slow from the 1970's average of 17 percent a year to 10-13 percent a year.

Countries that can afford to import more HVP's will do so, for the same reasons they initially entered the HVP market: to upgrade and diversify diets, to obtain semiprocessed items to process further, and to reduce food preparation time and labor as societies become more urbanized and affluent.

However, O'Brien says there's some evidence that the most affluent developed countries are becoming saturated with HVP's and won't be increasing purchases as rapidly in the future as during the 1970's. Instead, the expanding markets for American HVP's will be the high-income developing nations: the Middle Eastern OPEC countries, Hong Kong, Singapore, Taiwan, South Korea, Mexico, Venezuela, and the Caribbean countries with high tourism.

To expand the U.S. share of world HVP trade, we'll have to become much more aggressive marketers.

In addition, Eastern Europe could significantly increase HVP imports from the United States. But economic conditions in Eastern Europe would have to improve to allow policymakers there to boost HVP imports as a way to improve diets and reduce social and political unrest.

Higher Values, Faster Growth Rates Set HVP's Apart from LVP's

	Value per ton		Annual growth rate, 1970–80
	1970	1980	
	dollars		*percent*
LVP's			
Corn	70	140	7.5
Wheat	75	175	9.0
HVP's			
Oilmeal	85	215	9.5
Flour	90	285	12.0
Veg. oil	290	670	9.0
Wine	260	975	14.0
Poultry	670	1,470	8.5
Butter	730	2,465	14.0
Beef	910	2,590	11.0
Cheese	935	2,905	12.0

Among American products, fast growth is most likely for broilers, pork, oilseed meal and oil, cereal preparations, and fresh fruits and vegetables. American HVP exports have been dominated by semiprocessed products, but the direction of world trade is more to unprocessed and highly processed items.

Competing for Markets

O'Brien cautions that the United States can't sit back and expect its HVP sales to increase automatically.

"The American HVP export performance relates not so much to any limit on our capacity to produce competitively priced HVP products, but to more aggressive marketing and the use of promotion and export subsidies by competing HVP exporters, particularly the European Community," he says.

"To expand the U.S. share of world HVP trade, we'll have to become much more aggressive marketers."

Some of the ways the U.S. government could help accomplish this, he says, are:

• Putting more money and thought into HVP export promotion. With special funding earmarked for HVP export promotion, USDA's Market Development Program could expand marketing activities in high-growth areas abroad and improve the flow of market intelligence back to HVP exporters in the United States.

• Sharing some of the risks, and the considerable startup costs, that HVP producers must assume to enter the export market. The French government, for example, gave financial aid to livestock producers so they could build

special plants to conform to Muslim slaughter laws, important in the Mideast market. The U.S. government could offer similar assistance through tax credits, low-interest loans, and other means that do not amount to direct export subsidies.

• Providing loan guarantees or interest rate buy-downs for countries that wish to import American HVP's. This could be done under P.L. 480 and CCC export credit programs. The main objective would be to familiarize foreign buyers with our products. Many countries that received U.S. food aid in the 1950's and 1960's have become significant customers for U.S. bulk commodities—at full cash prices.

• Stationing USDA agricultural attaches in the developing countries that currently don't have attaches and that are potential high-growth customers—for example, the United Arab Emirates and many of the middle-income African countries. By being on the spot, attaches can provide important information on market opportunities, O'Brien says.

• Pressuring competitors to stop subsidizing HVP exports—particularly the European Community. This can be done through complaint procedures established in the General Agreement on Tariffs and Trade (GATT), as well as in other forums. Even stronger trade policy lobbying will be needed to expand the U.S. share of the HVP market than was necessary over the last two decades to increase our LVP trade, according to O'Brien. It's unlikely that we'll be able to end all unfair trade practices that are used in the HVP market, but we can attempt to reduce them, he says.

• Increasing the awareness of export markets by American HVP producers and processors, so that HVP trade opportunities aren't lost, by default, to foreign suppliers. □

[*Based on material provided by economist Patrick O'Brien of the International Economics Division, Economic Research Service.*]

Measuring the Benefits—and the Obstacles

How much difference does processing make in the payoff for exporters? In another study, ERS economists Gerald Schluter and Ken Clayton compared exporting $1 million worth of soybeans as beans versus exporting the same amount of beans as soymill products.

They calculated that exporting the processed commodity generated $2.8 million more in total sales throughout the economy. Processing also resulted in 48 more jobs, adding an extra $400,000 to household income.

The benefits of value-added exports increase when the product is more highly processed. Take $1 million worth of wheat exported as wheat versus the same amount of wheat exported as flour. The flour generates $8.8 million more in total sales, creates 192 extra jobs, and produces $1.9 million more in household income.

The most dramatic example in the Schluter and Clayton calculations is a comparison of $1 million worth of corn exported as corn versus the same amount of corn exported as dressed poultry. Such "processing" generates over $44 million more in total sales throughout the economy, 1,153 more jobs, and $9.3 million more in household income.

However, in both the O'Brien and Clayton-Schluter analyses, the economists are quick to point out that such gains are only *potentially* available. In reality, both physical and political obstacles restrain exports of U.S. processed products.

Physical obstacles include the location advantage that some of our HVP competitors have—for example, the EC's proximity to other European nations such as Sweden and Switzerland. Another physical problem is that the U.S. transportation system is geared more to shipping raw bulk commodities than to moving HVP's, which frequently require special handling.

But the physical problems are less troublesome than the political barriers that confront our HVP exports. Like the United States, foreign governments prefer to buy unprocessed products and let their citizens do the processing. So, they erect trade barriers to protect their domestic markets from imported HVP's.

The EC, which is the world's largest market for HVP's, limits foreign HVP imports by imposing both flat-rate tariffs and variable levies. The latter are designed to guarantee that an imported product is always priced higher than one produced within the Community.

The EC also presents the United States with a second kind of trade barrier—export subsidies that make it hard for U.S. producers to compete in third-country markets. EC export subsidies and processor subsidies (payments to compensate for the high price of processors' inputs) together grew about 25 percent a year between 1973 and 1980.

In 1980, the Community spent almost $220 million for direct subsidies of poultry exports, for example. The same year, its total HVP sales destined for non-EC countries came to $26 billion—and its total export subsidies reached $8 billion.

U.S. Beef: Pricing Itself Out of Mideast Markets

While the growing global appetite for beef is creating thriving import markets, American producers are missing the boat because their top-grade, feedlot-finished meat is too expensive.

USDA estimates that 3.3 million metric tons of beef were imported throughout the world in 1981. A decade earlier, world beef trade was only 2.3 million tons.

Much of that growth in world demand comes from developing nations where per capita incomes have risen along with newly acquired oil wealth or industrial expansion. People in these nations usually want to translate income gains into an improved diet.

The Mideast-North Africa region is a prime example of how beef demand has surged in the "Third World," according to economist John Parker of USDA's Economic Research Service. In 1975, the area imported 90,400 metric tons, or only 4 percent of world beef trade. Imports rose to 472,000 metric tons last year, and they are expected to exceed 600,000 metric tons this year—about 17 percent of world beef trade.

"The people expect to see some benefits from oil revenues," Parker says. "Enabling them to buy foods that they've never before been able to afford, such as meats, is an important way that these governments have shared oil revenues with their people."

Leading the expansion in Mideast-North African beef purchases is Egypt, whose imports grew from 17,600 metric tons in 1975 to a projected 175,000 metric tons this year. This would make Egypt the seventh largest importer behind the United States, Italy, France, the Soviet Union, the United Kingdom, and West Germany.

Disappointing Share

The U.S. beef industry might be expected to cash in on these fast-developing markets, but American beef is making only small gains.

U.S. beef is a specialty product. It's sold in restaurants and hotels that cater to foreigners.

"Most of the Mideast demand is for lower priced, low or medium quality beef," Parker says. Mideast governments are far more concerned with the nutritional value of beef than with its taste and texture.

U.S. producers finish most of their beef cattle in feedlots to achieve the high quality cuts that Americans demand. While taste and texture of feedlot-finished beef are far better, it cost about $5,000 a ton delivered to Cairo, compared with $1,900 a ton for Argentine beef last year.

"U.S. beef is a specialty product in the Middle East. It's sold in restaurants and hotels that cater to foreigners, particularly to Americans," Parker says.

"The beef that the Mideast people eat comes mostly from Argentina, Uruguay, Australia, Latin America, and the European Community," he adds, noting that many of these governments provide export subsidies to encourage sales, further undercutting high-priced U.S. beef exports.

Even so, Parker notes that U.S. beef exports increased 21 percent in value to $300 million in 1981, and our beef exports to Saudi Arabia nearly doubled in value, rising to $24 million."

Cultural Appetites

Despite the gains in Mideast beef imports, Mideastern people consumed only about 22 pounds of beef per capita last year, compared with about 80 pounds per American. While there may be considerable room for more beef in Mideast diets, meat consumption is also affected by historic cultural differences.

Beef is a traditional staple in North Africa, but mutton and lamb are preferred in the Mideast east of Suez.

These differences are reflected in beef imports. Egypt, which even in Biblical accounts took a dim view of sheep-raising cultures, imported more than 122,500 metric tons of beef and only 9,000 metric tons of mutton and lamb last year. On the other hand, Saudi Arabia imported 32,000 metric tons of lamb and mutton, 6 million sheep, and 46,000 metric tons of beef.

However, beef has an advantage over mutton and poultry that makes it attractive for customers in many developing nations, Parker says. Refrigeration is rare in delivery trucks in some countries, so meats often spoil en route from storage to the store.

A frozen side of beef, by virtue of its size, is far less likely to thaw and spoil than frozen chicken or mutton—the two major competing meats in the region. Pork is in little demand in Islamic countries due to religious restrictions.

Whatever the opportunities and obstacles for further expansion of Mideast beef markets, lack of foreign demand for U.S. beef is beside the point in one sense. America, the world's largest beef producer, is also the world's largest beef importer.

In fact, the United States imported an additional 1.3 billion pounds in 1981, mostly lower-grade beef for hamburgers and for processing into canned or frozen products. Australia, New Zealand, Argentina, and Canada provided most of our beef imports—valued at $1.4 billion last year.

Even so, stronger export markets could offer U.S. beef producers a means of supporting prices when the beef cycle is near its peak of output. On the other hand, the growing international demand could also drive up prices for the beef America imports. □

[Based on special material provided by economist John B. Parker of the International Economics Division, Economic Research Service.]

Up and Down Business Cycles Now Rock Rural Economy

The "sleepy village" image of rural towns may mask an economic revolution that is binding the prosperity of rural America ever more closely to swings in the overall U.S. economy—and making it more susceptible to consequences of economic policies and national trends.

A half century ago, a fourth of all Americans lived on farms, and in hundreds of counties farm residents made up the majority of the population.

Today, however, less than 8 percent of nonmetro employees work on farms as operators, hired workers, or unpaid family workers. Other sectors now provide most of the jobs. Manufacturing plants employ 22 percent of the nonmetro labor force, and about 60 percent is found in service-type industries such as transportation, communication and public utilities, wholesale and retail trade, and government.

The upshot of rising nonfarm employment is that the historic economic isolation of rural counties is quickly eroding. Evidence of this adjustment is found in the link between nonfarm rural employment and national economic cycles.

From 1969 to 1976, nonfarm employment in a large proportion of rural U.S. counties jumped up or down by at least 10 percent from year to year. The net shifts followed the cycle of U.S. industrial production.

Following the Trend

Three implications can be drawn:

- Nonfarm employment followed the national trend in most rural counties, regardless of size, location, or degree of rurality.
- Considerable year-to-year variability in nonfarm employment is common in rural counties.
- Nonfarm labor markets in rural areas as well as urban areas are sensitive to the swings in the national business cycle and to the national policies that influence it.

A half century ago, these conclusions might have been dismissed for their limited relevance to the rural economy. But, today, nonfarm economic activities greatly affect rural counties. In fact, a large part of total personal income in rural counties now comes from nonfarm sources.

Even among farm families, income earned from nonfarm activities is often crucial. About 62 percent of farm operators' income in 1980 was derived from nonfarm employment. Many families living on small farms have incomes approaching those of families living on much larger farms, thanks to off-farm jobs.

Other shifts in rural economies are also contributing to their new character. By 1981, 62 percent of work-aged people in nonmetro areas were in the labor force (either working or looking for jobs), up from 60 percent in 1973. Around 3.5 million women joined the nonmetro workforce during this period, as 3 out of each 5 new jobs in rural areas were taken by women.

New Rural Jobs

What are these new nonfarm rural jobs? Over one-fifth of the net increase in jobs during 1973-81 was in government—about the same share as for wholesale and retail trade. The largest gainer (about 30 percent of the net increase) was in other services such as motels, personal and business services, repair, and health.

The recent change that makes rural economies more similar to those of urban areas is the steady increase in the rural service sector, in various farm services, and even in skilled and professional jobs such as accountants and teachers.

An example of these changes can be seen in the growing rural presence of fast food franchises.

Today, 70 percent of all U.S. jobs are in the service sector. In nonmetro areas, service-producing jobs have increased from just over one-third of all jobs in 1940 to six-tenths of all jobs in 1981.

Although rural labor markets are becoming more sensitive to national economic policies, differences remain between urban and rural counties:

- The light, nondurable industries that are prevalent in rural areas tend to enter a recessionary period later, decline less, and recover faster than the heavy, smokestack industries found in cities.
- Service-type industries are affected last by business cycles because they tend to be small businesses in which proprietors can make quick decisions to minimize losses or earn early rewards during cycles. Also, they tend to deal in services that consumers have little ability to postpone, such as food retailing and medical services.
- Farming, which still undergirds the economy of many rural counties, usually continues to operate at near-normal levels in a recession, although equipment purchases and capital outlays may be deferred. However, the farming industry is becoming more closely linked to national money markets, and more subject to spiraling interest rates and to international commodity markets.

Despite such differences, the fact remains that rural economies are much more dependent on national economic policies than in the past, and they will probably become even more so as they continue to diversify. Monetary and fiscal policies that affect employment nationally will, thus, increasingly affect rural jobs.

As a result, rural people may become more interested in cushioning the effects of instability, uncertainty, and growth than in the old development policies directed toward remedying rural stagnation and decline. □

[*This special article was prepared by Lloyd D. Bender, an Economic Development Division economist stationed at the University of Montana, Bozeman, Mont.*]

A Vintage Time for American Wine?

Americans are raising their wine glasses more often—and roughly three out of four of those glasses are filled with U.S. wine.

Per capita wine consumption has been on the rise for many years. In the early 1970's, adult Americans drank an average of about 2.6 gallons a year per capita. By 1981, consumption had climbed to 3.3 gallons.

This translates into more winemaking and increased grape output, especially in California, the largest grape-producing state.

"A total of 506 million gallons of U.S. and imported wine were shipped throughout the country in 1981," says economist Ben Huang of USDA's Economic Research Service. "This was up 5 percent from 1980 and almost 14 percent from 1979."

Domestic shipments of U.S. wine rose to 391 million gallons last year and accounted for over 75 percent of the total.

Increased wine use may be partly due to more Americans taking up the European practice of drinking wine with meals, particularly dinner. But there are other reasons as well.

"Americans are becoming more knowledgeable about wines," says Jean Valentine of the Wine Institute. "Also, there's a trend away from the spirits (hard liquor), and more people are drinking wine as a beverage."

Spreading Vines

Cashing in on the boom, the wine industry has sharply expanded since the late 1960's, and growers have planted more acres of grapes. In California, which produced 90 percent of all U.S. grapes last year, wine grapes take up almost half of the total grape acreage.

"For example, the California acreage of wine grapes increased from about 337,000 in 1980 to around 343,000 last year," Huang says.

"However," he adds, "most of the expansion is due to a 38-percent increase in the acreage of young vines, some of which won't bear fruit for the next 3 years. The current bearing acreage has actually been decreasing over the last few years. Nevertheless, the new plants will ensure greater supplies in the future."

The main concern right now is competition from imports, which are capturing a larger share of the U.S. market.

Huang is optimistic that the market can absorb further increases in production. "Per capita wine consumption is still rising. The main concern right now is competition from imports, which are capturing a larger share of the U.S. market," he says. Imports accounted for 23 percent of last year's wine shipments to U.S. destinations, up from 16 percent in 1973.

1981 Crop Came Up Short

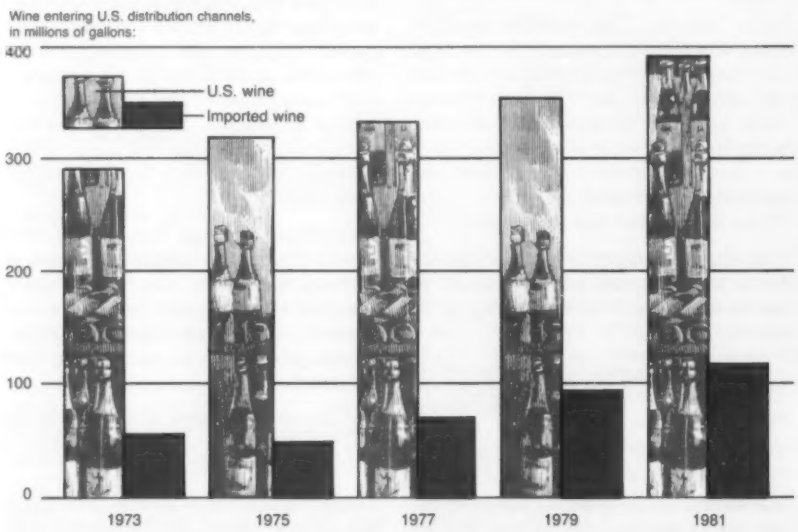
Even though the outlook is for larger production in the years ahead, last year's crop was smaller than 1980's output because of extremely hot and dry weather.

The California grape crop was only about 4 million tons, down more than 1 million tons from 1980. The production of wine grapes fell 11 percent to around 1.8 million tons.

However, winemakers continued to meet the high demand by diverting more grapes to wine use. The proportion of the total crop used for wine rose from 54 to 57 percent.

The 1982 crop looks more promising. An August survey placed California's total grape production at about 4.9 million tons. Wine grape production is projected at a record 2.1 million tons, 17 percent greater than last year and 5 percent above 1980's all-time high.

Domestic Shipments of U.S. and Imported Wines Are on the Rise, with U.S. Wines Still Holding a Big Lead



Because of this year's large crop, minimum guaranteed prices for Thompson seedless grapes are running about $150 a ton in the San Joaquin Valley, compared with a weighted average of $200 last year. French Colombard grapes are somewhat higher, $175 to $190, down from an average $244 last year. Prices could rise later in the season, but they won't go lower.

On the other hand, wine prices have been going up. According to the Bureau of Labor Statistics, wholesale prices for table and dessert wines increased 9 percent from July 1981 to July this year.

A Growing Competitor

Americans may like the home-grown product, but U.S. wines are relative newcomers to world markets. Can our wines compete against traditional European wines with reputations built up over several centuries?

U.S. wine exports are still fairly small, but they're growing fast. According to Huang, last year's exports rose 36 percent from a year earlier, to 10.7 million gallons, still only about 2 percent of U.S. wine production. Total value was $42 million, a 42-percent jump from 1980.

For years, Canada has been the largest export market for U.S. wine. According to the Wine Institute, that country bought more than 5.5 million gallons in 1981, up 20 percent from the previous year. England came in second with over a 100-percent gain, to more than 1 million gallons. Colombia ranked third with about 402,000 gallons—a 677-percent leap from the 51,708 it took in 1980.

The growing reputation of California wines, rising prices for traditional European wines, and vigorous sales campaigns by U.S. exporters and wineries are at least partly responsible for the increased export sales of U.S. wines. □

[*Based on material provided by economist Ben Huang of ERS' National Economics Division.*]

A Layman's Brief Guide to Wine

Wines fall into four basic classes: appetizer wines (like Sherry); red, white, and rose table wines; dessert wines (such as Port); and sparkling wines (mainly Champagne).

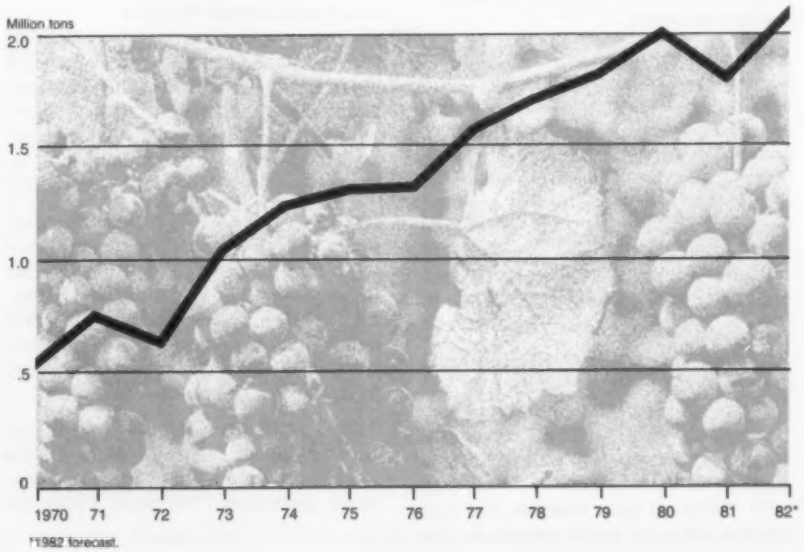
Wines are also classified into generic categories, such as Burgundy or Rhine. In addition to generic names, many are named for the grape from which they are made, for example, Cabernet Sauvignon. Under California and federal law, at least 75 percent of a bottle of wine bearing the name of a specific grape must be made from that grape variety.

The grape skins make the difference between red and white wines. The red is fermented with the skins, and the white isn't. Rose wines are made by allowing the juice to ferment with the skins for only a short time.

White wines are currently the most popular. According to industry data, shipments of these wines have increased more than 300 percent since 1974. White wines made up about 60 percent of all table wine shipments in 1981, almost double the 32 percent they registered 7 years earlier.

American wines come from two main types of grapes. Most California wines are made from varieties of grapes that were originally from Europe. Therefore, California wines taste much like their old-world counterparts. Wines from other states, such as New York or Washington, are made from native American grapes, so their flavor is different.

California Wine Grape Production. . . Heading for a Record Year



*1982 forecast.

Lean Years for U.S. Farmers

Large supplies and weak demand have produced declining prices in agriculture. The economy has advanced little since 1979, and bumper 1982 crops will add to already burdensome carryover stocks.

Some recent signs that the economy may be starting to perk up and that interest rates may be easing are far too uncertain yet to evaluate. These developments may provide the best hope for ultimate recovery of the farm sector, although—for the immediate future—they could probably offer only limited relief.

A few statistics provided by analysts of USDA's Economic Research Service help summarize economic conditions in the farm sector:

• *Farm incomes down.* Since 1979, the real (inflation-adjusted) incomes of U.S. farmers have fallen. Including the value of unsold crop and livestock inventories, real net farm income fell from $19.9 billion in 1979 to $13.0 billion last year—a decline of 35 percent. By way of comparison, after-tax corporate profits (adjusted for inflation) dropped 22 percent during this period.

• *Farmland values falling.* Declining incomes have contributed to declining land values. USDA's index of farm real estate values dropped 1 percent between February 1981 and April 1982. The downturn was more severe after taking inflation into account, and followed a 2-percent real decline between 1980 and 1981. However, farmland isn't the only real estate that's suffering; the real value of residential property fell 10 percent last year.

• *Machinery sales weak.* Farmers have been as reluctant to purchase new machinery as new land during this period. Unit sales of 2-wheel drive tractors fell 15 percent between 1979 and 1980 and another 13 percent between 1980 and 1981. Although weak incomes and high interest rates are major causes for the slack machinery sales, the continued inflation in prices hasn't helped. List prices rose 11 to 12 percent in 1980 and 8 to 9 percent last year.

Farmers' total cash receipts rose 9%, but costs climbed 19%.

• *Exports decline.* Exports represent another traditional source of strength that has weakened. After soaring a healthy 26 percent in fiscal 1980 and rising another 8 percent last year, the value of U.S. farm exports is forecast to slip 8 percent this year—the first such decline since 1969. Weak economic growth abroad, the strong dollar, and large world crop supplies are contributing to this year's decline.

• *Foreclosures up.* With farmers' balance sheets deteriorating—equity value fell 2 percent last year, the first drop since 1961—forced sales and foreclosures have been rising. The number of foreclosures is still relatively small, however, with the Farmers' Home Administration estimating that fewer than 3 FmHA borrowers per 1,000 are in foreclosure.

The Fundamental Problem

Put in the simplest terms, the erosion of farmers' financial well-being since 1979 reflects the failure of farm prices to keep pace with rapidly rising production expenses. Whereas farmers' total cash receipts have risen 9 percent since 1979, their costs have climbed 19 percent.

Nearly all of the upward push on costs has come from inputs produced off the farm. Between 1979 and 1981, the cost of nonfarm inputs (such as fuel, fertilizer, pesticides, labor, and machine hire) soared nearly 30 percent, while the cost of inputs originating on the farm—feed, livestock, and seed—fell 5 percent.

This cost disparity between farm and nonfarm inputs has implications for the relative financial health of crop and livestock producers. The main inputs for livestock production are feed and feeder livestock—inputs of farm origin. Crop production, on the other hand, is more heavily dependent on nonfarm inputs.

Despite these differences, livestock and crop farmers have both been hit by escalating costs for two vital inputs, fuels and interest. Together, fuel and interest charges were responsible for nearly half the total rise in production expenses from 1979 to 1981. They now take a larger chunk of farmers' outlays than any other single category—and the proportion is still growing.

As in the general economy, the 1979-80 doubling of oil prices accelerated cost inflation for farmers. Expenses for fuels and oil jumped 36 percent between 1978 and 1979, and another 29 percent the following year. By 1981, they had doubled. Although fuels make up only 6.6 percent of farmers' total costs, the higher oil prices also pushed up the cost of fertilizer, pesticides, and other manufactured items.

Interest expenses have grown even more dramatically since 1979. Farmers' outlays for short-term interest soared 65 percent from 1979 to 1981, while the cost of real estate interest jumped 45 percent. Total interest expenses now account for 14 percent of total production costs, up from 10 percent in 1978 and 7.5 percent in 1972.

Downward Price Pressure

Fast-rising expenses are only a problem if farm prices don't keep up. The downward pressure on farm prices has come from several sources. Beginning in 1980, livestock prices weakened sharply in the first half, reflecting record-large meat output. Especially hard hit were poultry and pork producers.

At the same time, large crop supplies here and abroad—coupled with the embargo on grain sales to the Soviet Union—dampened prices for grains and soybeans. The swift economic downturn in the spring of 1980 added to the farm economy's troubles.

The impact of high interest rates began to take its toll.

Although prices improved across the board in the second half of 1980, the gains came primarily at the expense of production disasters on the farm. A prolonged drought and heat cut crop yields and interrupted the flow of livestock to markets. An equally swift upturn in the general economy boosted demand in the second half, lending further strength to farm prices.

However, prices generally didn't go high enough to outweigh the smaller marketings, and farmers' incomes remained under pressure. By the end of the year, crop prices had leveled off, and livestock prices had slipped substantially from their earlier peaks.

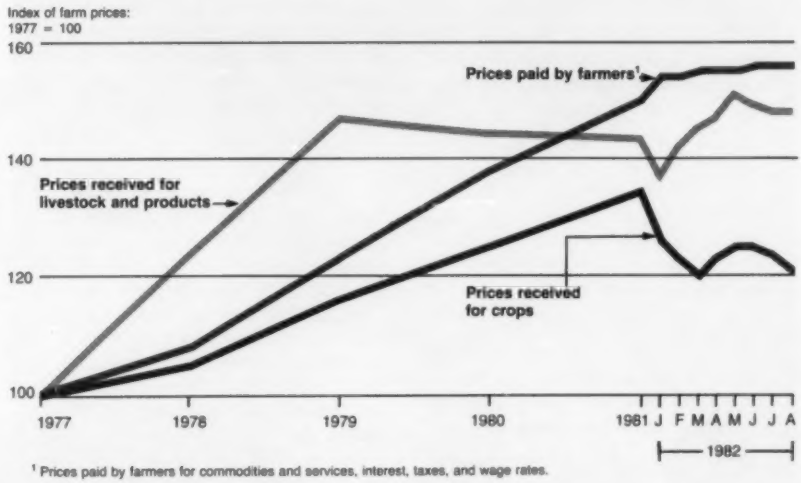
As 1981 began, the outlook appeared to be brightening. With exports up, the economy strengthening, and crop supplies diminished, farm prices for crops were forecast to resume their upward push. However, the impact of a year's worth of high interest rates began to take its toll.

High interest rates dampen demand, especially for price-sensitive raw commodities, by increasing the cost of holding inventories. This is true for domestic as well as foreign buyers, who then keep their inventories as lean as possible. Thus, the storage costs are passed back to farmers. While other producers of raw products—in the mining and steel industries, for example—can react by closing down plants and lowering production, most farmers don't have this option.

By drawing foreign funds to U.S. investments, high interest rates also boost the value of the dollar. This either raises prices of U.S. farm goods to foreign buyers or—as in 1981—keeps our prices from falling as fast abroad as they do at home.

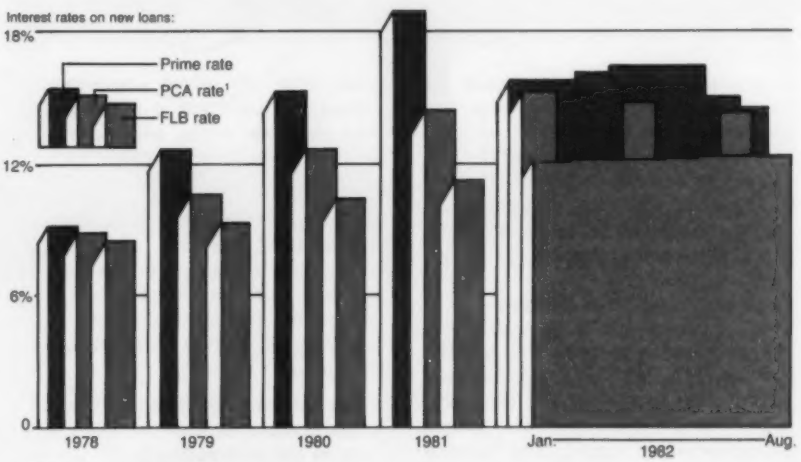
(Continued on next page)

Fundamental Problem: The Failure of Farm Prices—Particularly for Crops—To Keep Pace with Rising Production Expenses



[1] Prices paid by farmers for commodities and services, interest, taxes, and wage rates.

Some Easing in the Prime Hasn't Yet Given Farmers Any Significant Relief from High Interest Rates



[1] PCA rate on non-real estate loans.

Farm Income Update

Although inflation in production expenses has slowed substantially and livestock prices have improved since earlier this year, the outlook is for 1982 net farm income to be lower than in 1981.

Livestock receipts are forecast at a record $70 billion, up 2 percent from 1981, but crop receipts may drop 4 percent to around $72 billion. As a result, total cash receipts from farm marketings will probably be down about 1 percent this year.

On the other hand, direct government payments to farmers are estimated to total about $4 billion by the end of this calendar year, more than double those of recent years.

Farmers' production expenses are expected to rise only 2 percent in 1982, compared with 9 percent last year and 10 percent in 1980. This would be the smallest increase since 1964.

If these expectations are realized, net cash income to the farm sector should total $31 billion, compared with $31.5 billion in 1981. When adjusted for loan receipts, rental income, and capital expenditures, net cash flow is forecast at about $36 billion, compared with $36.8 billion last year.

Allowing for noncash incomes and expenses, and inventory adjustments, net farm income—the traditional income measure—is projected at about $19 billion this year, down from $25.1 billion in 1981 and $20.1 billion in 1980. Before inventory adjustment, net farm income will still likely be $19 billion, compared with $19.6 billion last year and $24.4 billion in 1980.

Major uncertainties surrounding these September forecasts: fourth quarter crop conditions, crop and livestock prices later this year, advance direct payments to participants in 1983 commodity programs, and production expenses.

At a time when foreign economies are weak and world crop supplies large, this can result in smaller U.S. farm exports. And with exports now one of the key sources of demand for the farm economy, any slippage there puts downward pressure on farm prices—especially for wheat, corn, and soybeans.

Huge Harvests, Weak Demand

Thus, rising interest rates hit the farm economy with a vengeance in the first half of 1981, offsetting relatively high crop prices. In the second half, however, the pressure on farm prices strengthened as record crop harvests and renewed recession had their impact.

During the summer, crop prices plunged on the news that record or near-record crops of soybeans, wheat, corn, sorghum, rice, and cotton would be harvested. And even with these large supplies and lower prices, exports failed to respond as expected.

Grain exports weakened substantially throughout the summer as foreign buyers awaited the new, lower priced crops, then picked up in the fall—but not enough to help farm prices much. Meanwhile, interest rates peaked in the third quarter, with the prime rate topping 21 percent.

Crop farmers responded by placing large portions of their harvests under loan to the Commodity Credit Corporation or in the farmer-owned reserves, in hopes of getting higher prices later on. However, the general economy began a renewed swing into recession. By then, the damage to crop prices had been done, but the recession—coupled with seasonal increases in meat output—caused livestock prices to fall.

After being stung by losses in 1980, hog producers succeeded in lowering output substantially last year, and hog prices strengthened during the summer. As the recession began, however, farm prices for all categories of livestock weakened—with broilers and hogs especially hard hit.

Bright Spots?

So far this year, some cause for optimism has appeared alongside the continued negatives of still-high interest rates, weak exports, and recession-dampened domestic demand. Interest rates have shown recent signs of easing, and some economic indicators suggest that the economy may be starting on the road to recovery.

In the farm sector, prices for livestock products have improved since last December, aided by sharply smaller production of pork. Although it's uncertain whether these gains can be sustained without recovery in the general economy, livestock producers overall are in better financial shape than during 1980-81.

Also benefiting farmers is the marked slowdown in cost inflation. By June, prices paid by farmers for all production items were up only 4 percent from a year ago. As recently as the summer of 1981, they were increasing at a double-digit pace.

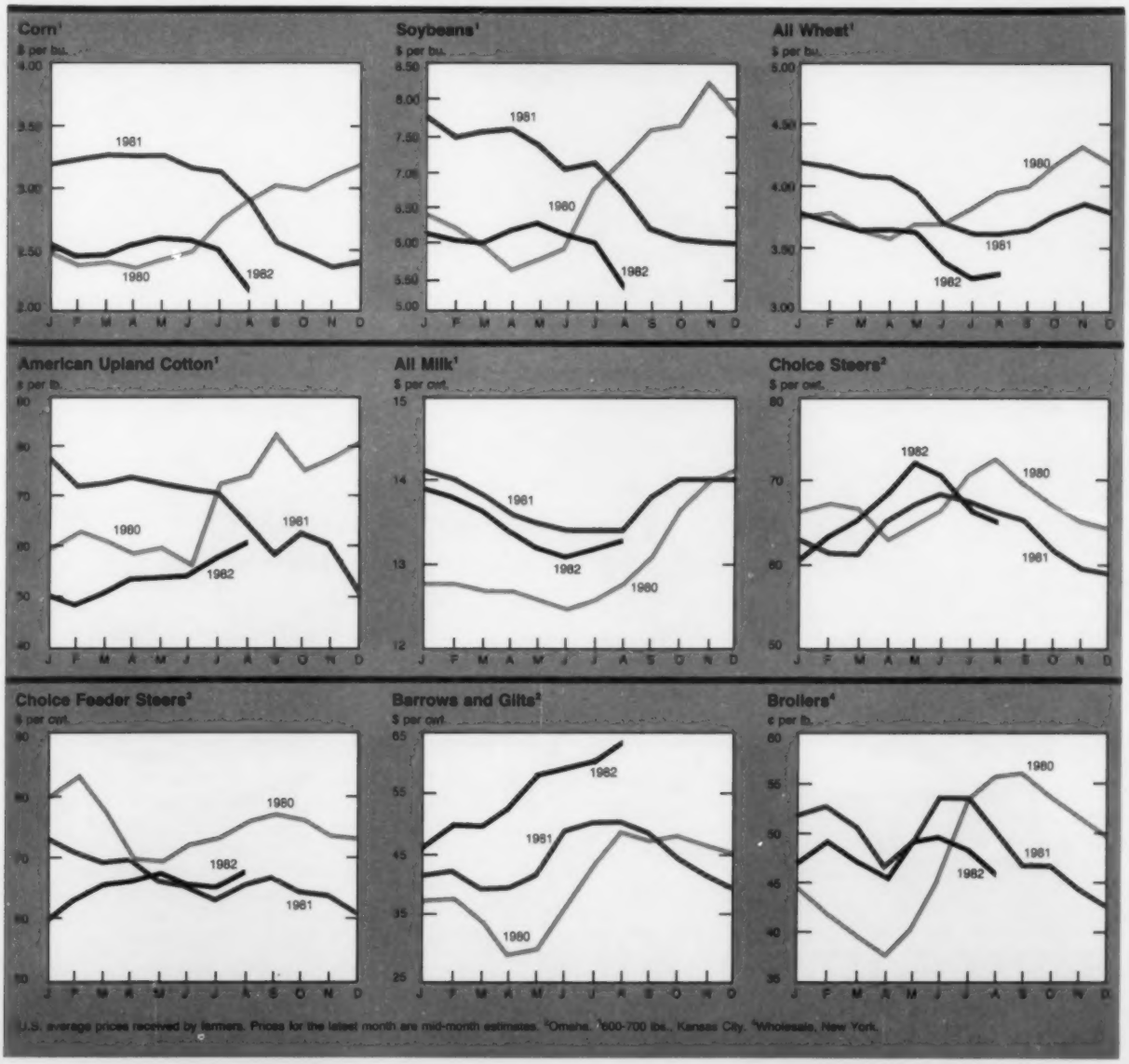
However, crop farmers have not seen the price gains livestock producers have realized. In fact, crop prices have weakened, in many cases further tightening the cost-price squeeze. Without stronger demand—from domestic as well as foreign users—this year's large harvests will add to the supplies remaining from last year's crops and continue to depress market prices. □

[*Based on material supplied by economist Lorna Aldrich and other analysts of the National Economics Division, Economic Research Service.*]

FARMLINE TRENDS

Monthly Price Monitor

Corn and soybean prices declined sharply from July to mid-August. U.S. average farm prices for corn dropped 31¢ to $2.19 per bushel—the lowest since February 1979. Soybean prices dropped 60¢ to $5.39, the lowest since October 1977. Farm prices rose for wheat, cotton, and milk, but remained below year-earlier levels. Among livestock, prices of Choice steers and broilers fell in August, but Choice feeder steers gained $2.74 per cwt. after a 2-month decline. Omaha barrow and gilt prices rose more than $3 to $63.51, up $12 from August 1981 prices.



U.S. average prices received by farmers. Prices for the latest month are mid-month estimates. [2]Omaha. [3]600-700 lbs., Kansas City. [4]Wholesale, New York.

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